HEALTHIER, LONGER,
BETTER LIVES

All things about life insurance inside SMSFs

March 2021

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Investment strategy

- Insurance must be considered & decision recorded

- Penalty = $4,440 to corporate trustee or to each individual trustee (up to $17,760)!

SIS alignment

- With 4 conditions of release
  - Second line of defence

Common hiccups

Insurance-only super fund

$1.5m Life cover

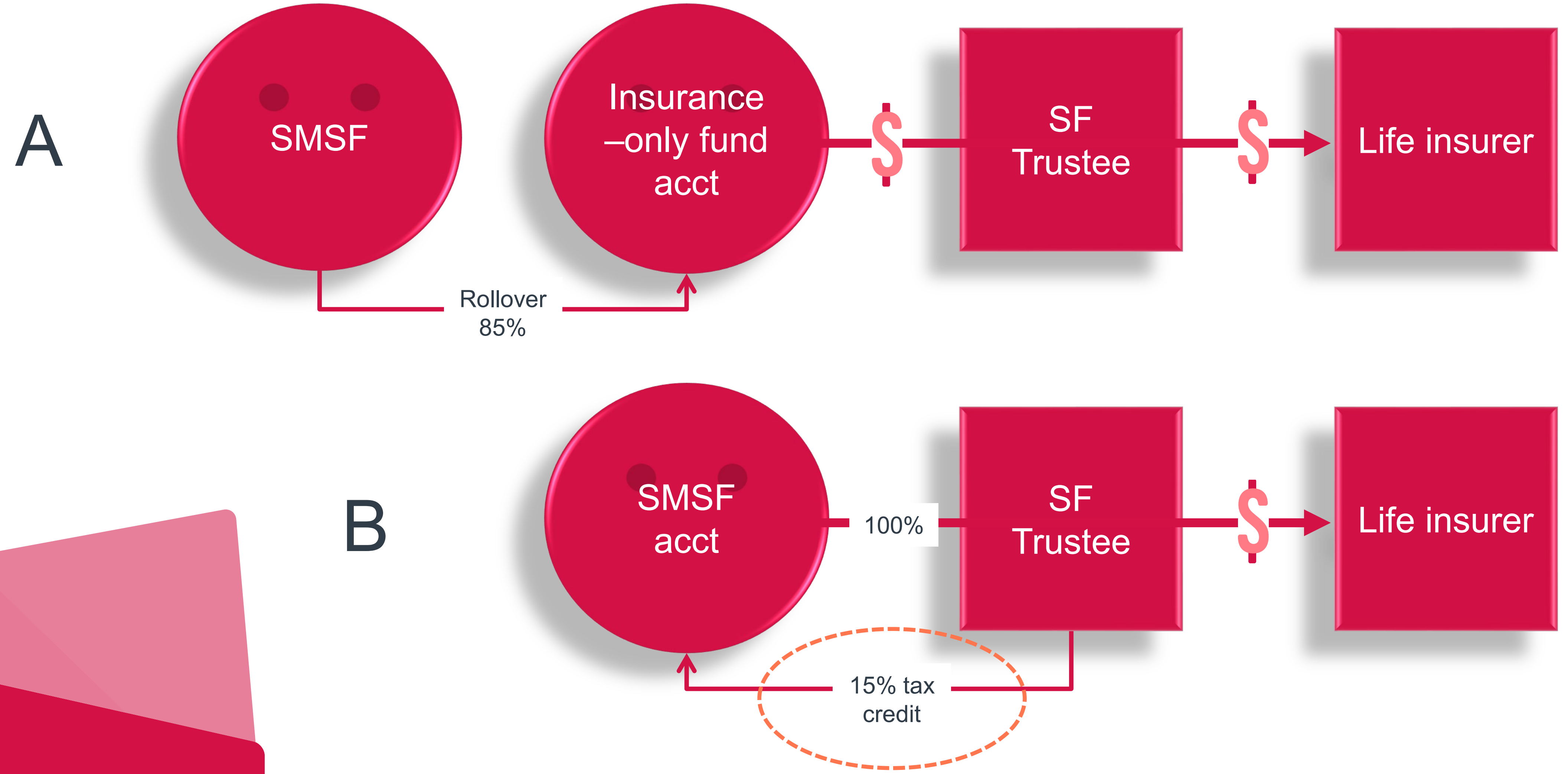
Intention is to rollover 85%

SMSF

But 100% of premium inadvertently debited from client's credit card

- Refund unlikely

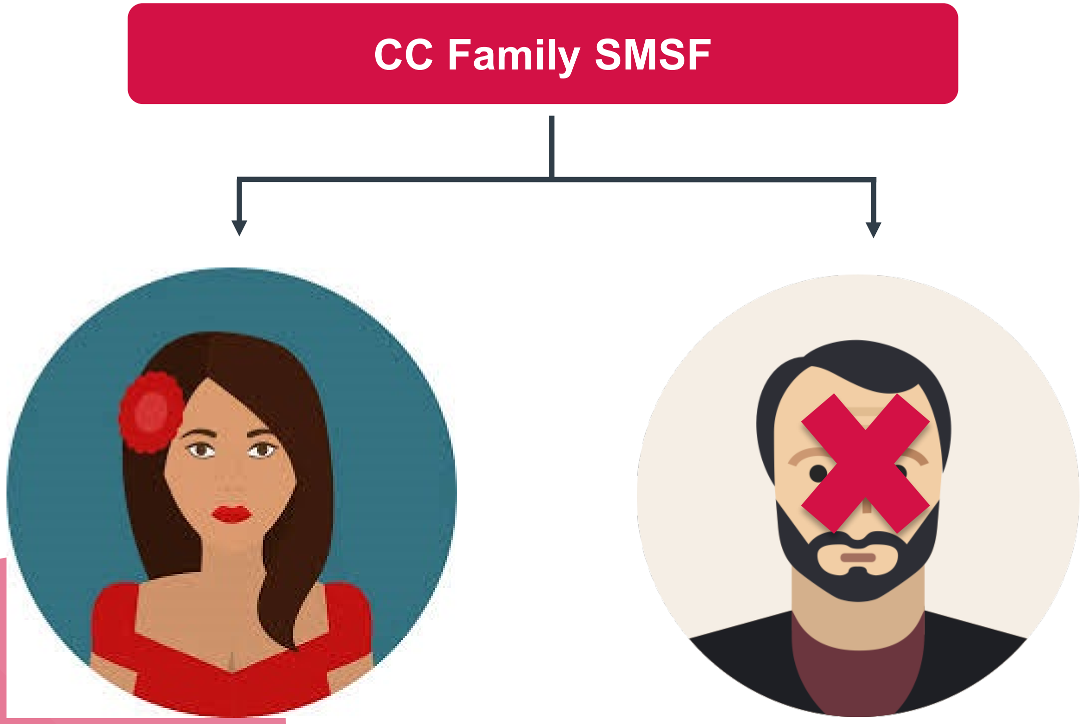
SMSF v risk-only



‘Future liability’ deduction

- If insurance in an SMSF
- Life insured employed and dies/TPD before 65
- SMSF to stay ‘alive’ post death

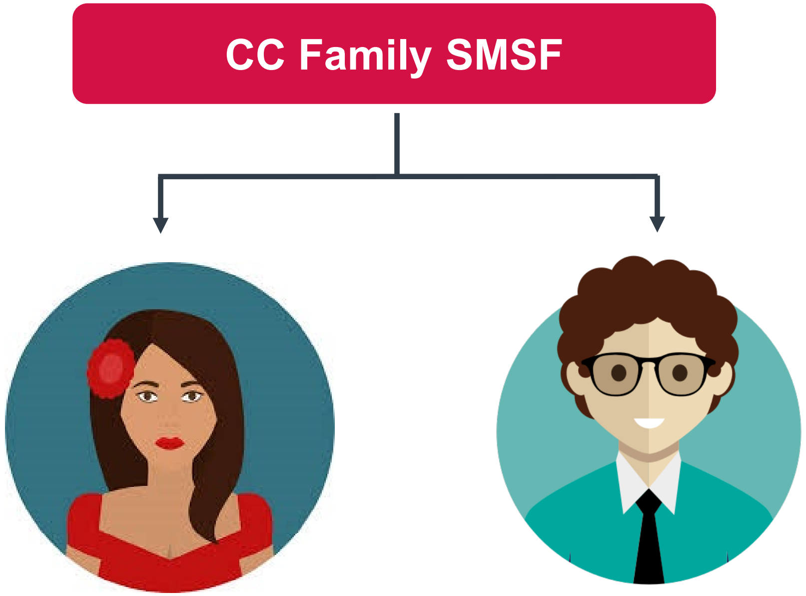
Example



- Carlos dies at age 50
- Service period = 15 years
- Total death benefit (incl insurance) = $2,450,000
- Claim tax deduction for premiums or elect for future service deduction?

‘Future liability’ deduction

- If insurance in an SMSF ✓
- Life insured employed and dies/TPD before 65 ✓
- SMSF to stay ‘alive’ post death ?



Adult son Cristian joins SMSF

Tax deduction = benefit amount x (future service days / total service days)

$2,450,000 x (15 years / 30 years)

$1,225,000

‘Future liability’ deduction - takeaway

- s295-470 ITAA 1997
- SMSF member passes away / tpd’d
- Insurance in SMSF
- SMSF to remain active

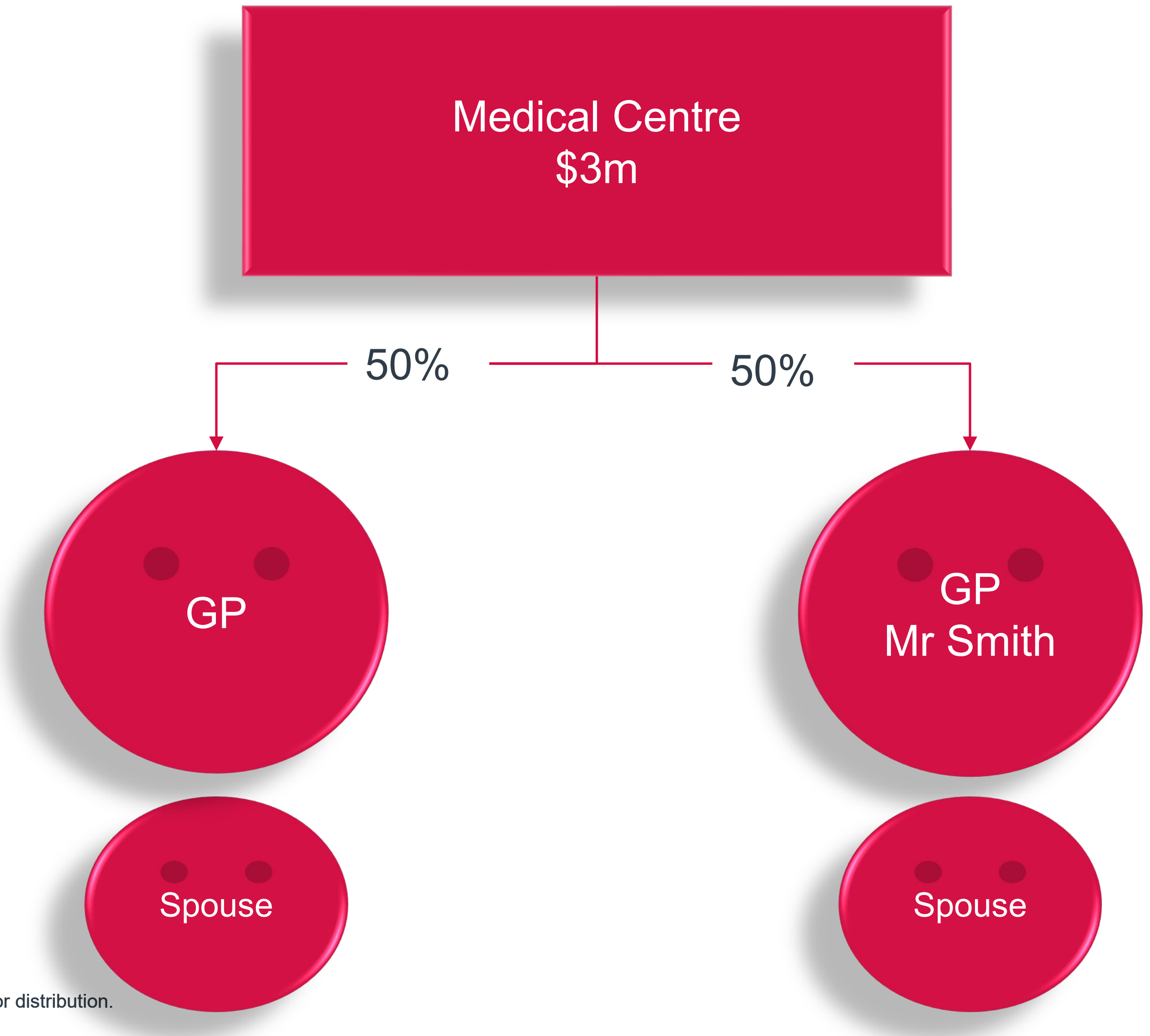
Mr and Mrs Smith
Personal Balance sheet

Assets		Liabilities	
Home	1,800,000	Home mortgage	Nil
Lifestyle assets	200,000		
Cash at bank	70,000		
Managed Discretionary Account Portfolio	1,800,000		
Investment Property	1,000,000	Investment Property Loan	700,000
50% shareholding in medical practice	1,500,000		
SMSF - Mr Smith - Mrs Smith	 1,500,000 1,100,000		

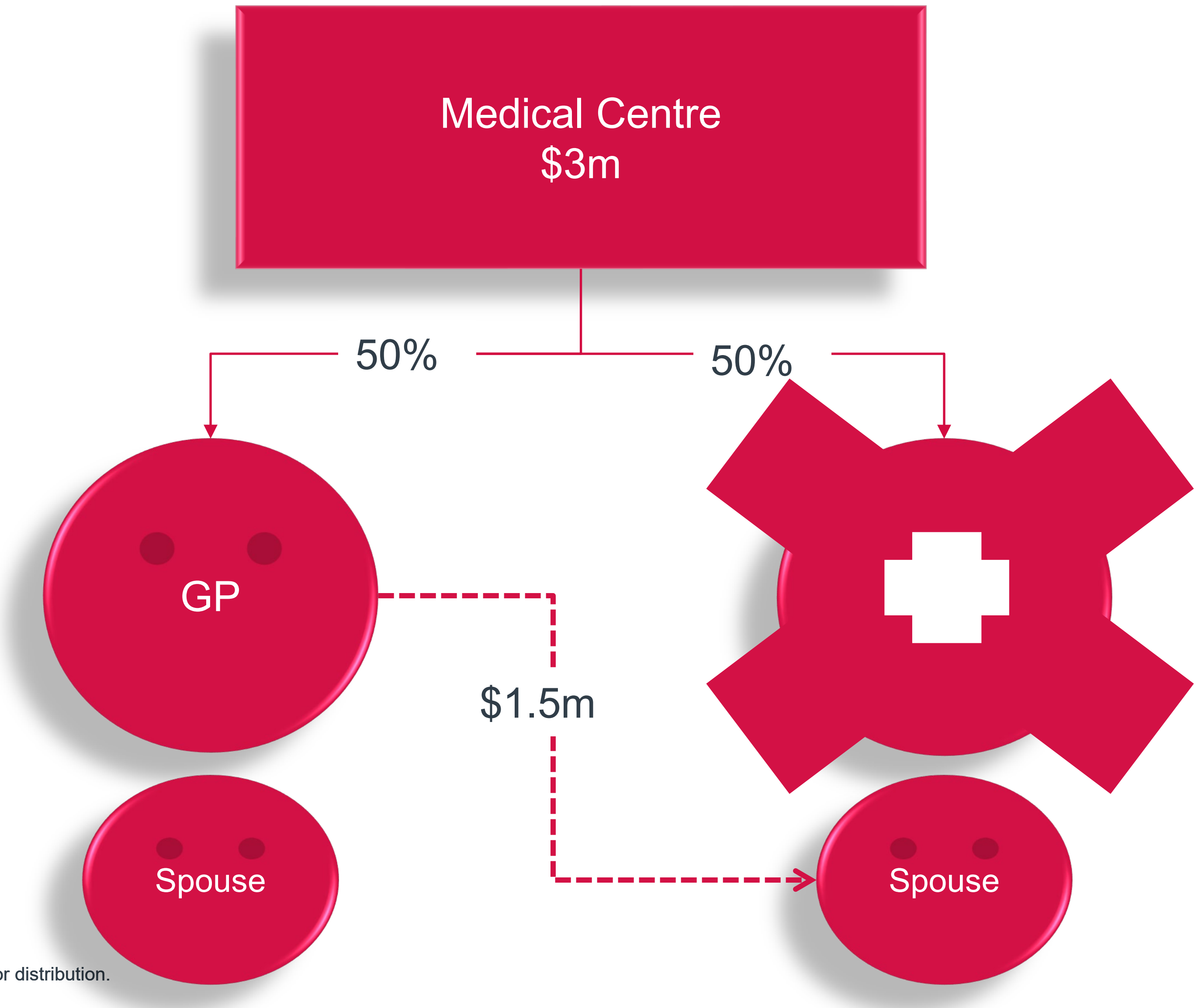
Seemingly no need for life cover as non-deductible debt nil…

…however what happens to the shares upon a premature death/tpd?

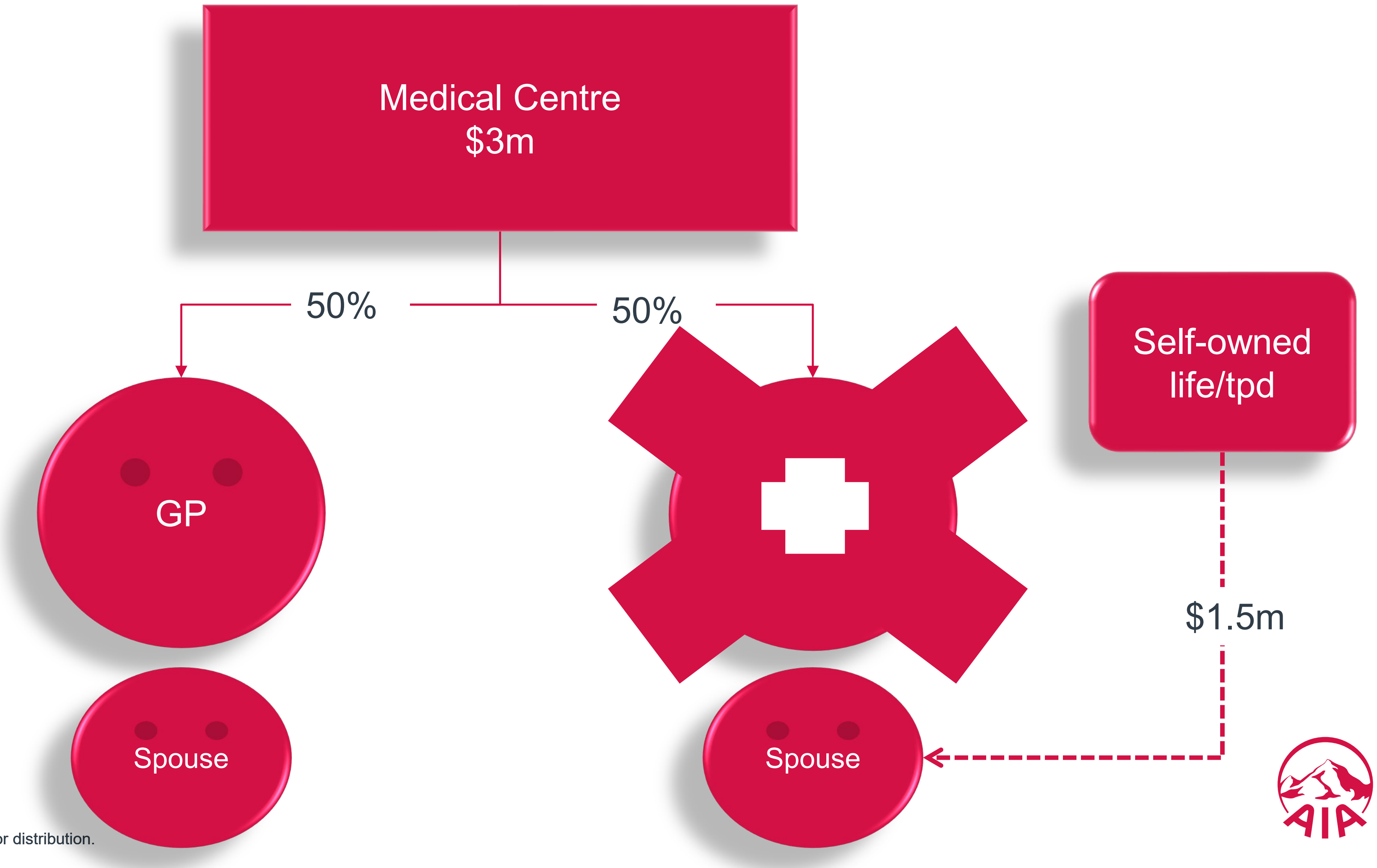
Buy/sell 101



Buy/sell 101

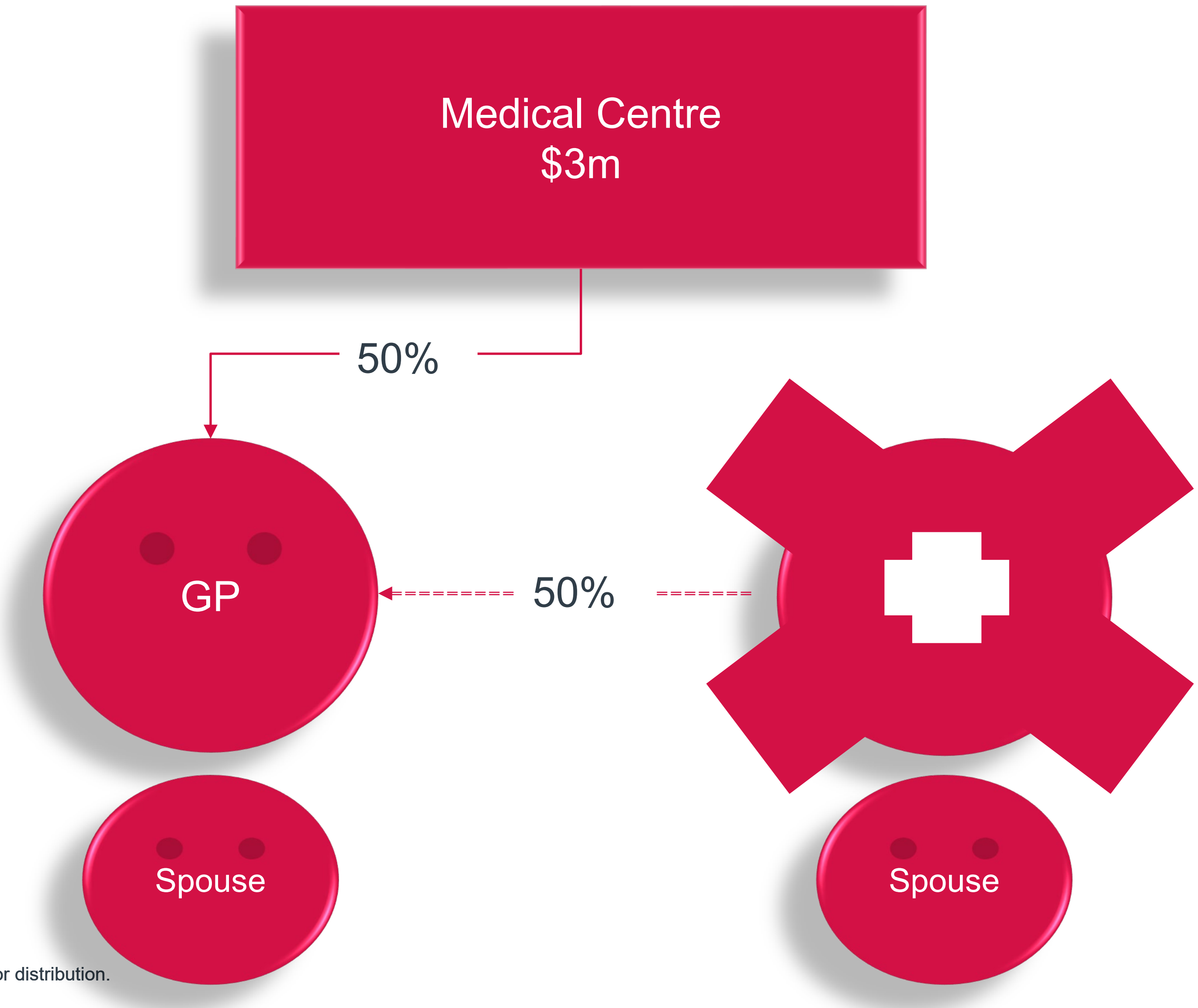


Buy/sell 101

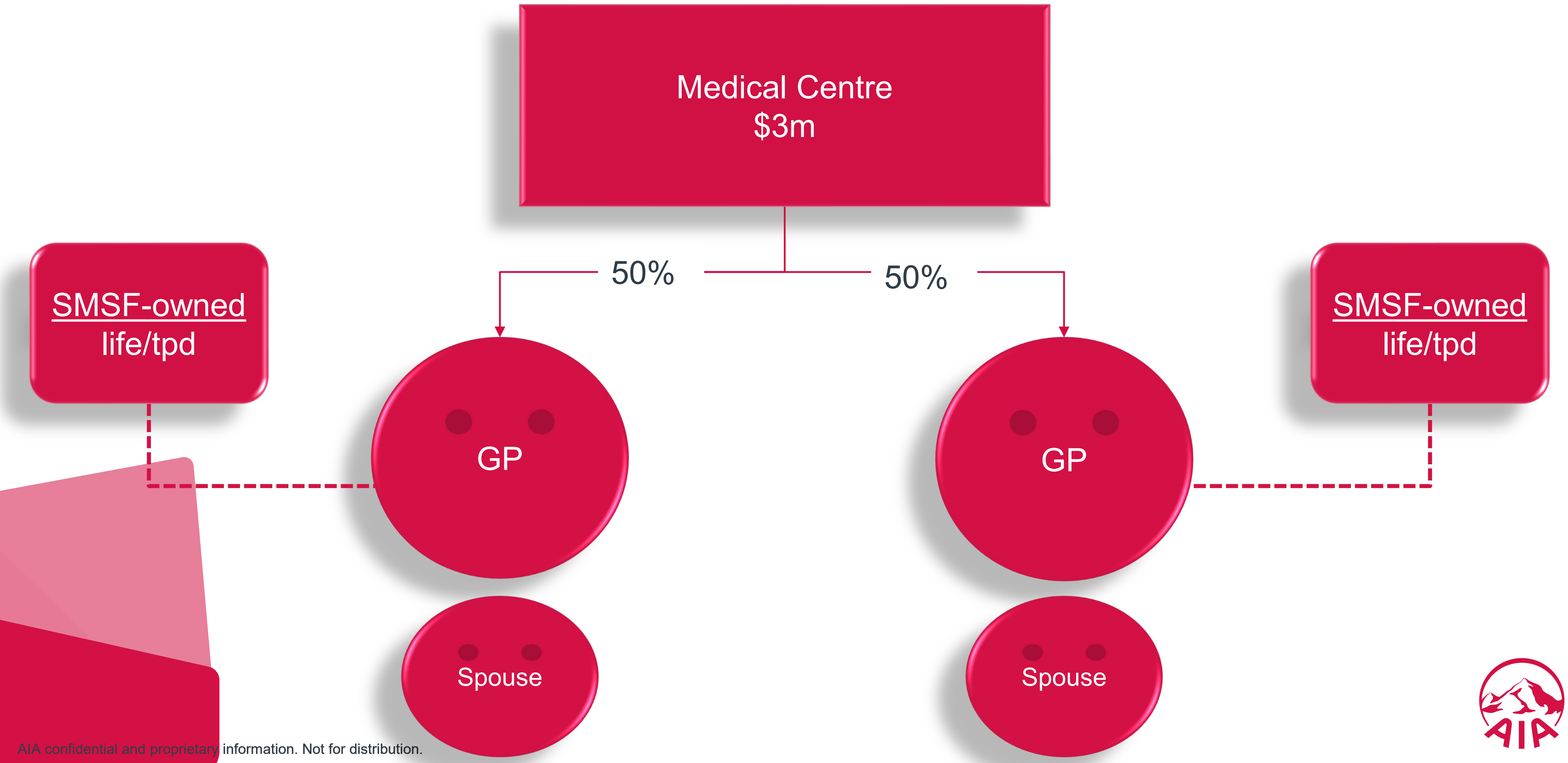


Medical Centre
$3m
50%
50%
GP
Spouse
Spouse
Self-owned
life/tpd
$1.5m

Buy/sell 101



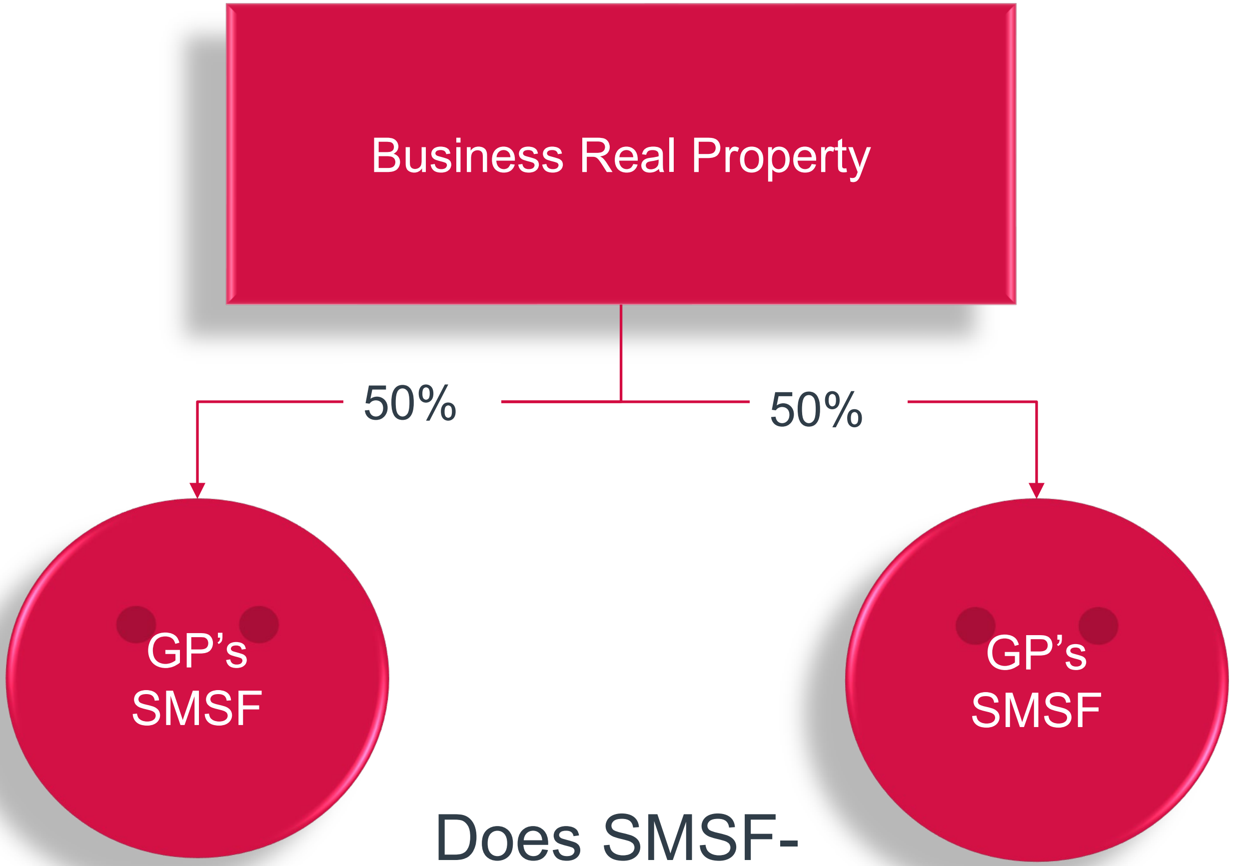
SMSF-owned cover?!



SMSF-owned buy/sell

- Avoid, if possible (ATO ID)
- Self-owned, with premiums funded from company trading account
- Otherwise, private ruling
- Check licensee standards

SMSF Liquidity



Does SMSF-owned insurance help?

BRP – SMSF owns cover

Assets		Liab + Equity	
Business Real Property	800	LRBA	(500)
Cash	200		
		Dad	250
		Mum	250

BRP – SMSF owns cover

Assets		Liab + Equity	
Business Real Property	800	LRBA	(500)
Cash	200		
Proceeds from life cover	$\boxed{500}$	Dad	250 + $\boxed{500}$
		Mum	250

BRP – SMSF owns cover

Assets		Liab + Equity	
Business Real Property	800	LRBA	(500)
Cash	200		
Proceeds from life cover	500	Dad	250 + 500
		Mum	250

BRP – SMSF owns cover

Assets		Liab + Equity	
Business Real Property	800	~~LRBA~~	~~Nil~~
Cash	200		
~~Proceeds from life cover~~	~~nil~~	Dad	250 + 500
		Mum	250

BRP – SMSF owns cover

Assets		Liab + Equity	
Business Real Property	800	~~LRBA~~	~~Nil~~
Cash	200		
~~Proceeds from life cover~~	~~nil~~	Dad	250 + 500
		Mum	250

Still need to pay a $750k death benefit!

Cross owned (non-super) by business partners

Assets		Liab + Equity	
Business Real Property	800	LRBA	(500)
Cash	200		
		Dad	250
		Mum	250

Cross owned by business partners

Assets		Liab + Equity	
~~Business Real Property~~	~~800~~	LRBA	(500)
Cash	200		
Cash (consideration for purchase of BRP interest)	800	Dad	250
		Mum	250

Surviving GP uses <u>ordinary</u> life proceeds to acquire BRP interest from SMSF

Cross owned by business partners

Assets		Liab + Equity	
~~Business Real Property~~	~~800~~	LRBA	$\boxed{\text{Nil}}$
Cash	200		
Cash (consideration for purchase of BRP interest)	$\boxed{300}$	Dad	250
		Mum	250

Liquidity for SMSF with BRP

- Fund-owned life cover likely to be unworkable

- Consider insurance outside the SMSF

Residential Property – SMSF owns cover

Assets		Liab + Equity	
Residential Property	800	LRBA	(500)
Cash	200		
		Dad	250
		Mum	250

Residential Property – SMSF owns cover

Assets		Liab + Equity	
Residential Property	800	LRBA	(500)
Cash	200		
Proceeds from life policy	500	Dad	250 + 500
		Mum	250

Residential Property – SMSF owns cover

Assets		Liab + Equity	
Residential Property	800	LRBA	(500)
Cash	200		
Proceeds from life policy	500	Dad	250 + 500
		Mum	250

Residential Property – SMSF owns cover

Assets		Liab + Equity	
Residential Property	800	~~LRBA~~	~~Nil~~
Cash	200		
~~Proceeds from life policy~~	~~Nil~~	Dad	250 + 500
		Mum	250

SMSF-owned cover - workable - in a Mum/Dad SMSF

Non-tax dependants

- s307-290 ITAA 1997 – SMSF trustee elects, from inception, not to claim premiums as deduction

- Avoiding untaxed element

Practical application

- Blended family
- Client (50) wants $1m insurance = adult biological children as beneficiaries
- Super-owned cover
- Annual premium = $1,200
- Already has $1.2m in SMSF
- ESP = 1/1/96

Untaxed element

Year	2	4	6	8	10
Foregone tax benefit – not claiming premium (cumulative)	421	1008	1811	2921	4397
Tax on untaxed element avoided	227,993	192,899	157,852	122,758	87,711
Actual tax payable – adult beneficiaries	121,121	102,477	83,859	65,215	46,596
Net benefit	**106,871**	**90,421**	**73,993**	**57,542**	**41,114**

Auto-reversionary - SMSF

Day 1

$1.5m Income stream commences – auto-reversionary – life cover paid from pension acct

Day 420

Primary pensioner passes away. Pension auto-reverts to surviving spouse

Pension = $1.55m

Day 440

$1m life proceeds paid into pension account

Day 785

Credit to reversionary pensioner's TBC = $1.55m

Actual pension balance = c.$2.5m

HEALTHIER, LONGER, BETTER LIVES

Thank you

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Google “AIA TECE” for resources